

THE LEONARD LETTER

A weekly electronic newsletter

from

*Bill Leonard, Member
State Board of Equalization*

November 10, 2003

*"History fails to record a single precedent in which nations subject to moral decay have not passed into political & economic decline." Gen. Douglas MacArthur (1880-1964)
WWII Supreme Allied Commander of the Southwest Pacific, Supreme United Nations
Commander*

UNDER THE DOME

*****TEACHERS ATTACK PROP. 13*****

Last week the California Teachers Association announced that it is sponsoring a November 2004 ballot measure to change Proposition 13 and increase property taxes on commercial property. The teachers say the additional money will be used for teacher salaries, smaller class sizes and more preschools.

The CTA may find their cry of poverty falls on deaf ears. In the 2003-04 budget, base K-12 education spending increased 6.7%. Total K-12 spending increased \$1.3 billion over the previous year, and total per-pupil spending is now more than \$9,300. The problems with public schools are not because there is not enough money spent in education; the problems arise from spending money in the wrong places.

Consider the Sacramento Bee's series investigating categorical spending earlier this year (http://www.sacbee.com/content/news/projects/paying_for_schools/story/6049346p-7005565c.html). The Bee found that more than \$12 billion is spent on more than 100 specific programs, but that, "The distribution of categorical money from district to district is uneven, with politics often determining who gets the most cash. A lot of the money is doled out based on outdated programs and formulas with little connection to modern-day needs in schools. And much of the money flows year after year with little or no state monitoring of whether the programs are working, or even happening. And some are not."

Rather than advocate for eliminating these ineffective programs and putting the money directly into classrooms now, the CTA is spending its time and its members' dues to try to raise your taxes. Not only is a great amount of commercial property owned by small businesspeople in California, but all businessowners will have to increase their costs to you, the consumer, to cover their increased tax bills.

*****LEVEL PLAYING FIELD*****

Taxpayers are not only annoyed when government misspends their tax money; they are also annoyed by people who do not obey the same tax laws that apply to everyone. To that end, I co-hosted a conference last week to discuss the Underground Economy. This topic grows more important as we face severe budget crunches because it is generally agreed that we could balance our budget if the proper taxes were collected from those who cheat on California's tax laws. The public needs to better understand the harmful consequences of paying cash under the table to workers, using unlicensed contractors, and engaging in retail sales without collecting sales taxes. The workers, the licensed contractors, and retailers who comply with these laws are all harmed when others do not follow the laws. It is the duty of government to enforce these laws for the benefit of all.

This enforcement needs to be tempered with justice. Those who commit fraud by knowingly and willingly violating these laws should be punished fully. But others seem to violate these laws out of pure ignorance, and the priority here should be to collect the taxes and pay the benefits to make things whole for the victim. The toughest situation to enforce is when both parties agree to ignore the law. It is hard to have sympathy for the worker as a victim when the worker has agreed or even offered to be paid under the table. Penalizing the employer alone is not justice in these instances.

California labor law, contractor license and tax compliance investigators are overburdened with the sheer numbers of laws and nuances that they must enforce. The Legislature and the Governor should review these laws and set priorities for law enforcement. Laws that are unenforceable only engender disrespect for all laws and take away from the ability to help the victims of illegal business practices.

To report a business that you believe is not complying with payroll tax laws, call EDD's Underground Economy hotline at 1-800-528-1783. To report sales tax evasion, call the BoE hotline at 1-888-334-3300. For concerns about unlicensed contractors, call the Contractors State License Board at 1-800-321-CSLB.

*****The Controller and the MIC*****

The Manufacturers Investment Credit (MIC) was signed into law in 1993 to encourage growth in manufacturing and employment. The MIC provides a six percent tax credit on costs of manufacturing equipment. The law states that the credit ends when it is determined that the number of manufacturing jobs is 100,000 less than the number of jobs in 1994. To me this is backwards. If the number of jobs is less than in 1994, then such incentives are needed more than ever. Nonetheless, last February, the Employment Development Department of Governor Davis concluded that California had in fact reached the sorry state of having 100,000 + fewer manufacturing jobs than in 1994, and therefore the MIC will expire on January 1, 2004.

Several bills were introduced last session to extend the credit but none even made it out of committee in their house of origin. Imagine my surprise when State Controller Steve Westly seemed to announce to a manufacturing group that not only was the MIC not expiring, but he also took credit for getting the Legislature to extend it. I hope that Westly is successful in convincing enough Democrats in the Legislature of the benefits of an investment credit for manufacturing. It is an important concept that should receive bipartisan support.

ISSUE FOCUS

***** The Time Has Come for Laffer's Bold Ideas*****

God bless Arthur Laffer. There was a wonderful profile of the 63 year-old economist in Thursday's LA Times and it could not have come at a better time. He is most famous for arguing during the Reagan administration that when taxes are raised too high, tax receipts come down. In other words, there is such a thing as a level of optimal taxation where services can be funded and economic behavior is allowed to flourish. What seems obvious now was widely disputed at that time, but Reagan's own income tax reductions and the corresponding increase in revenues provided solid proof of the theory.

Laffer argues that our progressive taxation system -- where people who earn more pay a higher rate -- is largely responsible for our current fiscal calamity because such progressive taxes guarantee huge volatility in revenues. It is virtually impossible in a political culture such as ours to make our spending mimic these swings; thus we repeat the cycle of fiscal crisis again and again because the massive increases in spending from the good years cannot be sustained in bad economic times. The obvious solution is a flat tax, with all Californians paying the same rate with few, if any, deductions. The rich would still pay more because they make more. The benefits would be that we could make long-term spending plans with much greater confidence, and our economy would almost certainly boom.

It is an undeniable fact that progressive taxation provokes high-earners to make choices that are in their own interest, rather than in the interest of the communities that are charging them comparatively higher tax rates. Those who do not understand this, I invite to take a Sunday drive through Incline Village, Nevada and check out the popular tax haven for scores of wealthy former Californians.

Laffer's proposal in full would essentially abolish every state and local tax in California, replacing them with a rate of about 6% on income for all Californians. The state would divvy up the amount based on population, the number of school age children, and other factors. The state's economy is picking up, as are revenues. That is why we must start this discussion immediately, or we will have to do so after the next budget meltdown that will surely come.

MISCELLANY

Three More Words to Know

Each week, the Leonard Letter features a few of the words from a list of 100 words that some educators say every high school student should know. The full list may be viewed at

http://www.houghtonmifflinbooks.com/booksellers/press_release/100words/.

67. Parameter (n)--- One of a set of measurable factors, such as temperature and pressure, that define a system and determine its behavior and are varied in an experiment; a factor that determines a range of variations; a boundary: *In politics, as in science, it is necessary to define the parameters of the situation, but it will take some time before all of the variables that contribute to the Schwarzenegger administration are known let alone measurable.*

68. Pecuniary (adj) --- Of or relating to money: *Governor-elect Schwarzenegger's biggest challenges are pecuniary, although the recent wildfires also present issues relating to forest management, environmental concerns and emergency resources.*

69. Photosynthesis (n) --- The process in green plants and certain other organisms by which carbohydrates are synthesized from carbon dioxide and water using light as an energy source. Most forms of photosynthesis release oxygen as a byproduct: *Noxious weeds are particularly efficient at photosynthesis and their quick growth crowds out native plants from being re-established after a wildfire.*

BOE AND LEGISLATIVE DATES

November 11 --- Veteran's Day

November 15 --- Statement of the Vote --- The last day for the Secretary of State to prepare, certify, and file a statement of the Vote.

November 17 --- Swearing-in of Governor Schwarzenegger.

November 18 & 19 --- BoE meets in Sacramento.

November 24 --- Sales and Use Taxes: October prepayment for fourth quarter is due. Special relief in the form of one-month extension of time to file and pay taxes or fees is available in those are (Los Angeles, Riverside, San Bernardino, San Diego, and Ventura) the Governor has declared a state of emergency for those who are unable to pay their taxes on time due to the recent wildfires. To request an extension, you must file two

forms, BoE 468, Request for Extension, and BoE 27, Penalty and Interest Relief for Disaster Victims. Both are available at www.boe.ca.gov. Or by calling 1-800-400-7115.

December 4 --- BoE meets in Sacramento.

January 5, 2004 --- Legislature reconvenes.

NOTABLE DATES/ HISTORY

November 10, 1775 --- The U.S. Marines were organized under authority of the Continental Congress. The Marines went out of existence after the end of the Revolutionary War in April of 1783. The Marine Corps were formally re-established on July 11, 1798. Sorry Marines, but there was a 15-year period where our nation did not have the benefit of your services.

November 10, 1770 --- French philosopher Voltaire, 75, uttered his famous remark: 'If God did not exist, it would be necessary to invent him.'

November 12, 1815 --- Elizabeth Cady Stanton, suffragist, was born in Johnstown, NY

November 13, 1789 --- Ben Franklin wrote "Nothing . . . certain but death & taxes"

November 13, 1982 --- Vietnam War Memorial dedicated in Washington, D.C.

November 14, 1972 --- Dow Jones closed above 1,000 for first time (1003.16)

November 15, 1864 --- General Sherman burned Atlanta

November 15, 1626 --- The original Mayflower "pilgrims," having lived in their American colony for six years, bought out their London investors for 1,800 pounds

November 16, 1914 --- Federal Reserve System formally opened

GENERAL TAX INFORMATION

For answers to your general tax questions, call the Board of Equalization information center. Customer service representatives are available to help you from 8:00 a.m. to 5:00 p.m. Pacific time, Monday through Friday (except state holidays).

Toll-free number: 800-400-7115

TDD service for the hearing impaired

TDD phones: 800-735-2929

Voice phones: 800-735-2922

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